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What Has the Supreme Court Done - The Home Office Deductions Is Virtually Eliminated after Soliman

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WHAT HAS THE SUPREME COURT DONE? THE HOME OFFICE DEDUCTION IS VIRTUALLY ELIMINATED AFTER *SOLIMAN*

I. INTRODUCTION: PURPOSE AND SUMMARY

The purpose of this comment is to discuss the relatively short history of Internal Revenue Code § 280A and to discuss the cases leading up to the United States Supreme Court decision of *Commissioner v. Soliman*.[1] The scope of the discussion will be limited to I.R.C. § 280A(c)(1)(A), which provides for a home office deduction if the dwelling unit is exclusively used on a regular basis and is the principal place of business for any trade or business.[2]

As will be discussed below, the Supreme Court has developed various standards to determine whether a home office deduction will be allowed. The traditional test is an objective "focal point test." The modern test, however, under *Soliman* is a subjective test in which a court will consider two factors to determine whether the taxpayer's home is his principal place of business. The first factor is to determine the relative importance of the activities performed at each of the locations (if more than one). The second factor is to consider the amount of time spent at each place.

The *Soliman* case has significantly altered the course of the home office deduction. The Supreme Court has narrowed the window of this deduction in order to obtain fixed standards to allow or disallow a deduction.[3] This comment will argue that the application of this decision will result in an unequal impact among taxpayers solely for the purpose of judicial efficiency.

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[1] 113 S. Ct. 701 (1993).

[2] *See* I.R.C. § 280A(f)(1)(A) (West 1993). The term "dwelling unit" includes a house, apartment, condominium, mobile home, boat or similar property.

[3] Michael M. Meggard & Susan L. Meggard, *Supreme Court Narrows Home Office Deductions in Soliman*, 78 J. TAX'N 132 (Mar. 1993).

In addition, the decision and its impact on the availability of the home office deduction will be discussed in detail.

II. WHY HAVE A HOME OFFICE DEDUCTION?

A home office deduction allows an ordinary business person to deduct expenses that are directly related to his business.[4] A tax-paying business person may deduct his pro rata share of the utilities, repairs, insurance, and office fixtures.[5] The following hypothetical will help demonstrate the operation of the deduction:

> A school teacher operates a small antique business out of her home and desires to take a home office deduction for her back porch which she converted into a show room for the merchandise. Assume that 25% of the general expenses for the dwelling unit are attributable to the home office. The taxpayer's gross income and expenses for her business would break down as follows:

Gross Income $40,000

Home Office Expenses	Total	Allocable to Office (25% of dwelling unit expenses)
Interest and Property Taxes	8,000	2,000
Insurance, Utilities, Maintenance	2,000	500
Depreciation	6,000	1,500

Total Home Office Expenses ..... $4,000[6]

Without the enactment of I.R.C. § 280A, the aforementioned expenses would be non-deductible as merely constituting personal expenses.[7] The deductions would only be allowed if they could qualify as ordinary and necessary business expenses.[8] Section 280A, nevertheless, allows for the home office deduction. I.R.C. §§ 162(a) and 280A are similar in that their ultimate purpose is to allow deductions only for those expenses which are business oriented and not personal.

III. THE HISTORY AND ENACTMENT OF I.R.C. § 280A

Before Congress created the home office deduction through its enactment of I.R.C. § 280A, a deduction was only allowed for business purposes and

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[4] I.R.C. § 280A (West 1993).

[5] *See* Treas. Reg. § 1.280A-2(3) (1983).

[6] 1992 U.S. MASTER TAX GUIDE 255-58 (C.C.H. 1991) (facts and figures modified).

[7] I.R.C. § 262(a) (West 1993).

[8] I.R.C. § 162(a) & 167(a) (West 1993).

depreciation.[9] The following cases exemplify the different procedures used by the courts prior to the enactment of I.R.C. § 280A in 1976. Ultimately, these different tests have led to confusion concerning when a deduction would be allowed.

For example, in *Davis v. Commissioner*, the Tax Court disallowed a professor's deduction for a home study because the deductions were not for ordinary and necessary business expenses.[10] The professor built and furnished an office over his garage to use as his study.[11] He used the study to grade papers and to prepare for his lectures.[12] The majority used a strict interpretation of the Code and refused to allow the deduction because it was not an ordinary and necessary business expense. The court reasoned that the expenses were more personal than business.[13] A strong dissent argued that the better standard to determine the availability of the deduction is the "appropriate and helpful" test.[14] This test, proposed by the dissenters, triggered the conflicting standards within the Tax Court and federal courts.[15]

The decision of *Bodzin v. Commissioner* exemplifies the inconsistencies between the Tax Court and the Courts of Appeals.[16] Ironically, Mr. Bodzin was an attorney–advisor in the office of the Chief Counsel of the Internal Revenue Service.[17] Bodzin lived in an apartment in which he used an 8x12 foot room as his study to keep up on current tax issues and matters related to his work.[18] Bodzin alleged that a mere $100 of his $2,100 for rent during the tax year of 1967 was attributable to his study and deducted it as a business expense. The Commissioner denied the deduction and the Tax Court reversed. The court held that the deduction qualified as an "appropriate and helpful" business expense.[19] The Fourth Circuit Court of Appeals reversed and concluded that

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[9] *Id.* A helpful summary of the cases before the enactment of § 280A is found in Karen O. Green, *Recent Cases and Rulings for the Income Taxation of Individuals*, 4 REV. OF TAX'N FOR INDIVIDUALS 366 (1980).

[10] 38 T.C. 175 (1962).

[11] *Id.* at 179.

[12] *Id.*

[13] *Id.*

[14] *Id.* at 180–88 (Raum, J., dissenting).

[15] *See* Newi v. Commissioner, 432 F.2d 998 (2d Cir. 1970) (affirming a Tax Court which followed the *Davis* dissenters and holding that an ABC television advertising salesman was entitled to a business deduction for his home office because it was both "appropriate and helpful").

[16] 60 T.C. 820 (1973), *rev'd*, 509 F.2d 679 (4th Cir.), *cert. denied*, 423 U.S. 825 (1975).

[17] *Id.* at 825.

[18] *Id.*

[19] *Id.*

Bodzin's apartment was simply not used as his place of business.[20] The appellate court's rationale for reversing the Tax Court was that he purely by choice elected to do some of his work at home, just as some lawyers and judges elect to do.[21] The court in essence avoided adopting one particular test.

The foregoing cases exemplify the different standards that courts have used when analyzing a potential deduction for a home office or study. The standards range from "ordinary and necessary" to "appropriate and helpful" to a complete avoidance of the conflict.[22] The conflicting standards have never provided taxpayers with a relatively clear cut method to determine whether their offices qualified for a deduction. This problem led to the possibility of taxpayer abuse.

In order to rectify the potential for taxpayer abuse under the "appropriate and helpful" standard Congress enacted I.R.C. § 280A as part of the Tax Reform Act of 1976.[23] Specifically, the section begins with a general rule of exclusion and provides:

> (a) General rule.—Except as otherwise provided in this section, in the case of a taxpayer who is an individual or an S corporation, no deduction otherwise allowable under this chapter shall be allowed with respect to the use of a dwelling unit which is used by the taxpayer during the taxable year as a residence.[24]

After the general rule of exclusion the Code adopts three exceptions. I.R.C. § 280A(c)(1) provides the following exceptions:

> Subsection (a) shall not apply to any item to the extent such item is allocable to a portion of the dwelling unit which is exclusively used on a regular basis—
>
> > (A) the principal place of business for any trade or business of the taxpayer.
> >
> > (B) as a place of business which is used by patients, clients, or customers in meeting or dealing with the taxpayer in the normal course of his trade or business, or

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[20] 509 F.2d 679, 681 (4th Cir. 1971).

[21] *Id.* The Court also concluded that Mr. Bodzin's employer provided access to his office during the evenings and on the weekends. *Id.*

[22] *See* Davis v. Commissioner, 38 T.C. 175 (1962); Newi v. Commissioner, 432 F.2d 998 (2d Cir. 1970); Bodzin v. Commissioner, 60 T.C. 820 (1973), *rev'd*, 509 F.2d 679 (4th Cir.), *cert. denied*, 423 U.S. 825 (1975).

[23] Pub. L. No. 94–455, § 601, 90 Stat. 1520, 1569–72 (1977).

[24] I.R.C. § 280A(a). Treasury Regulation 1.280A–1(a) provides an additional requirement as follows:

> If a deduction is claimed for an item attributable to a dwelling unit used by the taxpayer during the taxable year as a residence, the tax payer must first establish that it is otherwise allowable as a deduction under chapter 1 of the Code before the provisions of section 280A become applicable.

> (C) in the case of a separate structure which is not attached to the dwelling unit, in connection with the taxpayer's trade or business.
>
> In the case of an employee, the preceding sentence shall apply only if the exclusive use referred to in the preceding sentence is for the convenience of the employer.[25]

In addition, the burden of proof is on the taxpayer to prove that his activities fit within one of the exceptions.[26] Additionally, this section provides that if the taxpayer is an employee, the deductions will only be allowed if the dwelling is used for the convenience of the employer.[27]

Despite Congress' attempt to clarify the availability of a home office deduction, I.R.C. § 280A has been subject to varying interpretations.[28] In essence, the Tax Court and Courts of Appeals have simply returned to the muddy waters of pre–§ 280A. In the seventeen years since the Tax Reform Act of 1976, the courts have failed to follow a clear cut rule for determining the availability of the home office deduction. The *Soliman* decision represents the United States Supreme Court's attempt to solve the home office deduction dilemma.

IV. Discussion of the Various Tests Used by the Courts to Determine the Availability of a Deduction Under I.R.C. § 280A(c)(1)(A)

There are two elements which must be satisfied in order for a court to allow a deduction under I.R.C. § 280A(c)(1)(A). First, the portion of the dwelling unit used by the taxpayer must be the principal place of business exclusively used as an office.[29] Second, the home office must be used for a trade or business.[30] The second element will be discussed first because it provides far less interpretive problems for the courts than the first element.

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[25]I.R.C. § 280A(c)(1) (West 1993).

[26]Welch v. Helvering, 290 U.S. 111 (1933). I.R.C. § 280A imposes heavy burden on taxpayers to prove that their home office expenses meet the stringent standards of deductibility. *See* Meiers v. Commissioner, 782 F.2d 75, 77 (7th Cir. 1986).

[27]*See* I.R.C. § 280A(c) (West 1993). While convenience of the employer is not defined in the Tax Code or its Regulations, there must at least be some showing that the offer is for the convenience of the employer. In *Drucker*, the Court of Appeals adopted the Tax Court's decision which concluded that the home office deduction would be denied because the taxpayer made "no showing that the office was used for the convenience of the employer." Drucker v. Commissioner, 715 F.2d 67, 69 (2d Cir. 1983).

[28]The purpose of the Act was to provide more definitive rules relating to deductions attributable to the business use of homes. *See* Harris v. Commissioner, 46 T.C.M. (CCH) 1130 (1983) (quoting S. REP. No. 1236).

[29]I.R.C. § 280A(c)(1(A) (West 1993).

[30]*Id.*

The trade or business element of I.R.C. § 280A(c)(1)(A) is not defined in the Code or the Treasury Regulations.[31] However the courts will undertake an analysis of several factors in order to reach a conclusion regarding the alleged business activity. For example, in *Moller v. Commissioner*, the Court of Appeals for the Federal Circuit analyzed several factors and ultimately denied a home office deduction.[32] The taxpayers, Mr. and Mrs. Moller, devoted their full–time work to their investment activities which included the management of four portfolios of stocks and bonds.[33] Each worked approximately forty hours a week and kept regular office hours.[34] The taxpayers filed a joint income tax return and claimed deductions attributable to maintaining the taxpayer's two offices in the amount of approximately $7,500 for the tax years of 1976 and 1977.[35] The IRS disallowed the deductions, but the Claims Court held that they were engaged in a trade or business and entitled to a deduction under I.R.C. § 280A.[36]

The Court of Appeals reversed and determined that the Mollers were investors, not traders, and that their activities did not amount to a trade or business.[37] The court did, however, recognize that the Mollers' investment activities were continuous, regular and extensive.[38] Ironically, the court held that this was insufficient in light of the nature of their investments.[39] The court focused on the fact that their income was derived from the long term holding of securities and not short term trading.[40] In essence, the court simply reasoned that the home office deduction was only for the production of income and not for a trade or business.

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[31] Section 162(a) does provide some guidance if the expenses are ordinary and necessary. Under this section, a deduction will be allowed for all expenses that are ordinarily and necessarily paid or incurred during the taxable year in carrying on any trade or business. I.R.C. § 162(a) (West 1993). The expenditures must directly relate to the trade or business and include the following: management expenses, commissions, labor, supplies, incidental repairs, operating expenses of an automobile used in the trade or business, travelling expenses, advertising, and insurance premiums. *See* Treas. Reg. 1.162–1(a)(1988). This list is by no means exhaustive of the available deductible expenses. I.R.C. § 263(a) limits section 162(a) by not allowing a deduction for capital expenditures for new buildings, permanent improvements or betterments made to increase the value of property. I.R.C. § 263(a) (West 1993).

[32] 721 F.2d 810, 815 (Fed. Cir. 1983).

[33] *Id.* at 811.

[34] *Id.*

[35] *Id.* at 812.

[36] *Id.*

[37] Moller v. Commissioner, 721 F.2d 810, 815 (Fed. Cir. 1983).

[38] *Id.*

[39] *Id.*

[40] *Id.*

The court's analysis was improper. The court should have avoided its attempt at distinguishing between traders and investors by declaring that the expenses were personal in nature. Section 262(a) of the Code prohibits deductions that are for "personal, living or family expenses." The Mollers' expenses should have been denied under this theory because the investment portfolios were their personal ones. They did not manage or solicit business from other individuals. It is this type of interpretive problems which has led the courts to develop inefficient methods of determining deductibility.

The courts, nevertheless, still participate in intricate line drawing regarding the trade or business element. In *Gaiewski v. Commissioner*,[41] the Second Circuit Court of Appeals disallowed a home office deduction for a full-time gambler because he was not engaged in a trade or business.[42] The court looked to three considerations: 1) whether the taxpayer is regularly and actively involved in the activity; 2) whether he holds himself out to others as engaged in the selling of goods and services; and 3) an analysis of the facts and circumstances surrounding the purported trade or business.[43] The court chose to focus on the second consideration because it was administratively fair and workable to taxpayers.[44] The court reasoned that the taxpayer only gambled for his own account and did not hold himself out as an operator of a bookmaking service.[45] He was, therefore, not engaged in a trade or business according to the Court.

Despite the *Gaiewski* court's attempt to create an administratively workable standard, the courts still maintain a case-by-case analysis as to what constitutes a trade or business. Both *Gaiewski* and *Moller* indicate that in the absence of workable standards, the courts must engage in line drawing that only serves to confuse taxpayers and tax-planners. This element has, however, produced far less confusion and inefficiency than the second element under I.R.C. § 280(c)(1)(A), namely, whether the portion of the dwelling unit used by the taxpayer is used exclusively as the principle place of business.

Once a court determines that taxpayers's activities are a trade or business, it will then determine whether the home office is the principal place of business.[46] It is this element which has produced the most litigation since the enactment of I.R.C. § 280A. The effects of this litigation culminated in the *Soliman* decision,

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[41] 723 F.2d 1062 (2d Cir. 1983).

[42] *Id.*

[43] *Id.* at 1065–66.

[44] *Id.* at 1067.

[45] *Id.*

[46] I.R.C. § 280A(c)(1) also requires an *exclusivity* element. Thus, an investigation may reveal that a purported office doubles as a den or guest room. This scenario would deny the deduction. *See* Hamacher v. Commissioner, 94 T.C. 348 (1990)(concluding that a taxpayer may conduct *more* than one business activity from a home office under I.R.C. § 280A(c)(1)). *But see* Green v. Commissioner, 78 T.C. 428 (1982)(concluding that a taxpayer can only have *one* principal place of business for each business in which he is engaged).

wherein the Supreme Court virtually eliminated the home office deduction by narrowing its availability through the application of a new subjective test.

The Treasury Regulations recommend a facts–and–circumstances analysis to determine the principal place of business when the taxpayer conducts his trade or business at more than one location.[47] Under the regulation, a court would consider several factors, including the total income attributable to each location and the facilities at each location. The facts–and–circumstances test was never formally adopted by the courts prior to *Soliman*, which involves an analysis of similar factors.

The predominant test the courts have elected to use to locate the principal place of business since the enactment of the home office deduction is the focal point test. Under the focal point test, a court will look to the location of each of the taxpayer's business activities.[48] A court will ultimately base its decision on where the goods and services are exchanged. The focal point test is an objective test because it involves an analysis of factors that are not subject to change based solely on a court's discretion.

In *Pomarantz v. Commissioner*[49] the Tax Court affirmed the Commissioner's finding of a tax deficiency because the taxpayer's home office did not qualify as the principal place of business under the tax code.[50] On appeal to the Ninth Circuit, the Tax Court judgment was affirmed.[51] The taxpayer in *Pomarantz* was a physician specializing in emergency care medicine.[52] He maintained a home office to keep his medical records and journals. In his office, he spent up to 250 hours per year reading medical journals and following up on patient care.[53]

The Ninth Circuit affirmed the Tax Court's use of the focal point test.[54] However, the appellate court concluded that under the focal point test the hospital, rather than the home, was the taxpayer's principal place of business.[55]

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[47]Treas. Reg. 1.280A–2(3) (1983).

[48]*See* Jackson v. Commissioner, 76 T.C. 696 (1981); and Baie v. Commissioner, 74 T.C. 105 (1980)(determining that Congress intended the focal point to be the location of the taxpayer's activities).

[49]867 F.2d 495 (9th Cir. 1988).

[50]*Id.*

[51]*Id.* at 497.

[52]*Id.* at 495.

[53]*Id.* Because the taxpayer in *Pomarantz* did not treat patients in his home, he avoided the possibility of a deduction under to I.R.C. § 280A(c)(1)(B), which allows for deductions where a dwelling unit is a place of business used by patients and clients.

[54]Pomarantz v. Commissioner, 867 F.2d 495, 497 (9th Cir. 1988). The court also noted that the taxpayer's deduction would fail under a test which analyzed the location of where the dominant portion of the work was accomplished.

[55]*Id. Pomarantz* is strikingly similar to *Soliman* both factually, and as an alternative test to the focal point test. Both cases resulted in a denial of the deduction.

The Court determined that Dr. Pomerantz's principle place of business was the hospital because he consistently spent more time on duty while at the hospital, rather than at home.[56]

In *Drucker v. Commissioner*[57] the Tax Court also used the focal point test to deny the taxpayer musician a home office deduction.[58] In *Drucker*, the taxpayer musician was a member of the Metropolitan Opera Orchestra in New York City and used a room in his five room apartment as his studio.[59] The musician used the home studio approximately thirty hours per week for practice.[60] The court used the focal point test and broke the activities down into three categories: practice, rehearsal and performance.[61] The court determined that the focal point of his activities was at Lincoln Center because his position as a member of the orchestra required him to rehearse and perform at Lincoln Center.[62] The court also determined that Lincoln Center was the location where the goods and services were exchanged.[63] The court did admit that the taxpayer's practice was essential to maintain his technical expertise.[64]

Both the *Pomarantz* court and the *Drucker* court recognized that some activities require organization and practice away from the focal point (principal place of business) of their activities.[65] These cases exemplify the Tax Court's unwillingness to succumb to a case–by–case subjective test.[66] In fact, Congress attempted to reject this analysis and provide clear objective guidelines to determine whether a home office deduction would be allowed.[67]

The objective focal point test was not without criticism. In *Drucker*, Judge Wilbur's dissent demonstrated, through the use of examples, that the objective

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[56]The Court emphasized that the very essence of the medical profession is based on treatment at the hospital and not studying or writing at home.

[57]79 T.C. 605 (1982), *rev'd*, 715 F.2d 67 (2d Cir. 1983).

[58]*Id.*

[59]*Id.* at 605–06.

[60]*Id.*

[61]*Id.*

[62]Drucker v. Commissioner, 79 T.C. 605, 605–06 (1982).

[63]*Id.*

[64]*Id.*

[65]Pomarantz v. Commissioner, 867 F.2d 495 (9th Cir. 1988); 79 T.C. 605 (1982).

[66]The Tax Court's decision in *Drucker* was reversed on appeal and the Court favored an alternative test which looked to the time and importance of the activities at the home. 715 F.2d 67 (2d Cir. 1983). In Weisman v. Commissioner, 751 F.2d 512 (2d Cir. 1984), the Court of Appeals again rejected the focal point test in favor of placing the emphasis where the dominant portion of his work is accomplished.

[67]H. R. REP. No. 658, 94th Cong., 2d Sess. 160, *reprinted in* 1976 U.S.C.C.A.N. 2897, 3054. *See also* Drucker v. Commissioner, 79 T.C. 605 (1982), *rev'd*, 715 F.2d 67 (2d Cir. 1983).

focal point test is deficient.[68] Judge Wilbur argued that the principal place of business of a lecturer is not the place of delivery but rather the location at which he creates his speeches.[69] Judge Wilbur also added that the principal place of business of an artist is neither the gallery nor the museum where his paintings are sold or exhibited, but rather, it is where he uses his "extraordinary skill practicing, experimenting, revising, and perfecting his craft."[70]

A further illustration of the problems of the focal point tests rests with the ubiquitous travelling salesman. A travelling salesman conducts most of his business on the road. It is on the road where his goods and service are exchanged. Under the focal point test, a court would undoubtedly determine that his principal place of business is on the road. The injustice exhibited here is that a salesman must have some type of home office in order to schedule appointments, solicit business, take care of bills and study new or competitive products. His home office is certainly relatively important to his business, yet a court will deny his deduction. Congress attempted to prevent taxpayer abuse by providing the guidelines for a home office deduction.[71] The salesman in this example is not abusing the potential deduction. As a travelling salesman, he would most likely prefer to be at home with his family rather than in an office away from home.

The tests that the courts have developed for both elements of the home office deduction have produced unjust results for many taxpayers. With the *Soliman* decision, the United States Supreme Court has effectively eliminated the availability of a home office deduction at the expense of the non–abusing taxpayers who maintain legitimate home offices.[72]

V. *SOLIMAN*: THE DECISION, IMPACT AND CRITICISM

The United States Supreme Court has narrowed the availability of the home office deduction by adopting a subjective test.[73] The Tax Court and the Fourth Circuit Court of Appeals, by using a facts–and–circumstances test, had left a window of opportunity open for those taxpayers who use a home office. The *Soliman* decision quickly shut this window without a justifiable rationale.[74]

The taxpayer in *Soliman* was a self–employed anesthesiologist who worked thirty to thirty-five hours per week, treating patients in three hospitals in the

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[68] Drucker v. Commissioner, 79 T.C. 605, 610 (1982), *rev'd* 715 F.2d 67 (2d Cir. 1983) (Wilbur, J., dissenting).

[69] *Id.*

[70] *Id.*

[71] I.R.C. § 280A(c)(1) (West 1993).

[72] Commissioner v. Soliman, 113 S. Ct. 701 (1993).

[73] *Id.*

[74] *See* Robert T. Kelly, Jr., *Home Office Deductions Restricted By Supreme Court*, 50 TAX'N FOR ACCT. 196 (1993); Michael M. Meggard & Susan L. Meggard, *Supreme Court Narrows Home Office Deductions in* Soliman, 78 J. TAX'N 132 (1993).

Maryland and Virginia area.[75] None of the three hospitals provided him with an office.[76] The taxpayer lived in a three bedroom condominium and used a spare bedroom exclusively as an office.[77] The taxpayer did not meet with the patients in his office; but he did spend two to three hours a day conducting the following activities:

1. Contacting patients, surgeons and hospitals;
2. maintaining billing records and patient logs;
3. preparing for treatments and presentations;
4. satisfying continuing medical education requirements; and
5. reading medical journals and books.[78]

The taxpayer claimed a deduction for the portion of the fees, utilities and depreciation attributable to his home office.[79] The Commissioner denied the deductions because the office was not his principal place of business.[80] The taxpayer filed a petition in the Tax Court seeking a review of the tax deficiency.[81] The Tax Court surprisingly abandoned the focal point test after citing its criticisms.[82] The Tax Court determined that the focal test point should be abandoned because its effect was to merge I.R.C. § 280A(c)(1)(A) with § 280A(c)(1)(B), when the two sub–sections were intended to be applied separately.[83] The Tax Court in its place created the "facts–and–circumstances" test.[84]

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[75] *Soliman*, 113 S. Ct. at 704.

[76] *Id.*

[77] *Id.*

[78] *Id.* In *Soliman*, the taxpayer did not fall under I.R.C. § 280A(c)(1)(B) or (C) because he did not treat patients in the same bedroom, and the office did not involve a separate structure.

[79] *Id.*

[80] Commissioner v. Soliman, 113 S. Ct. 701, 704 (1993).

[81] *Id.*

[82] Meiers v. Commissioner, 782 F.2d 75 (7th Cir. 1986) (stating that the focal point test is not fair to taxpayers because it places undue emphasis upon the location of where the goods and services are provided and not where the work is predominantly performed); Weisman v. Commissioner, 751 F.2d 512 (2d Cir. 1984) (criticizing the focal point test because it shifts attention to the place where the taxpaer's work is most visible, rather than where the dominant portion of this work is accomplished); Drucker v. Commissioner, 79 T.C. 605 (1982), *rev'd*, 715 F.2d 67 (2d Cir. 1983) (criticizing the application of the focal point test because "[b]oth in time and importance, home practice was the 'focal point' of the appellant musician's employment related activities").

[83] Soliman v. Commissioner, 94 T.C. 20 (1990), *aff'd*, 935 F.2d 52 (4th Cir. 1991), *rev'd*, 113 S. Ct. 701 (1993).

[84] *Soliman*, 935 F.2d 52, 54 (4th Cir. 1991).

The Court of Appeals, in its review of the Tax Court's decision, adopted the following factors which the Tax Court stated weighed heavily in favor of a finding that the home office was the taxpayer's principal place of business:

1. The office in the home is essential to the taxpayer's business;
2. he spends a substantial amount of time there; and
3. there is no other location available for the performance of the office functions of his business.[85]

The Court of Appeals affirmed the Tax Court's use of this new facts–and–circumstance test to hold that the doctor's principal place of business was his residence office, and accordingly, that he was entitled to a home office deduction.[86] The Supreme Court rejected the new facts–and–circumstances test, reversing the Court of Appeals, and denying the deduction.[87] In so doing, the Court adopted yet another test to determine the taxpayer's principal place of business.

The Court adopted a subjective test and stated that "we cannot develop an objective formula that yields a clear answer in every case."[88] Under the new subjective test, the Court requires that two primary factors must be considered to determine the principal place of business. First a court must consider the relative importance of the activities performed at each business location.[89] Second a court must determine the amount of time spent at each place conducting business.[90]

In determining the relative importance of the activities performed at each place, the Supreme Court rejected the focal point test as being too conclusive because it could be misleading.[91] Yet, the Court stated that great weight must be given to this factor.[92] In analyzing the time factor at each location, the Supreme Court stated that this element is of particular importance when the relative importance of the business location fails to give a definitive answer.[93] The Court's rationale behind denying the deduction in *Soliman* is that it determined that the most significant event was the actual treatment of the patients.[94] The Supreme Court accordingly held that the home office activities

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85 *Soliman*, 113 S. Ct. at 704.

86 *Soliman*, 935 F.2d at 55.

87 113 S. Ct. at 706–08.

88 *Id.* at 706.

89 *Id.*

90 *Id.*

91 *Id.*

92 Commissioner v. Soliman, 113 S. Ct. 701, 706 (1993).

93 *Id.* at 707.

94 *Id.* at 708.

must be regarded as far less important.[95] Considering the time element, the Court simply determined that 10–15 hours per week in the home office, as compared to the 30–35 hours per week at the three hospitals, was not sufficient to qualify the taxpayer for the home office deduction.[96]

The *Soliman* Court, by its implementation of the subjective test, has virtually extinguished the effectiveness of I.R.C. § 280A(c)(1)(A).[97] Only a very small number of the taxpayers who use a home office will be allowed a deduction. Furthermore, the *Soliman* decision has been subject to great criticism because it has not clarified the muddy waters of the home office deduction.

Justice Stevens, dissenting in *Soliman*, began the criticism.[98] Justice Stevens emphasized that the purpose of the I.R.C. § 280A(c)(1)(A) standard is to prevent abuse and not to deny valid deductions.[99] Justice Stevens favored the proposed test by the Tax Court and Court of Appeals because it is virtually incapable of abuse.[100] The key factor emphasized by Justice Stevens was that the home office must be the only office available to the taxpayer.[101]

In addition to Justice Sevens' dissent, there are recent commentators who criticize the *Soliman* decision.[102] Specifically, one commentator provided a list of individual taxpayers who would be affected most by the new standard.[103] Taxpayers greatly affected include individuals in the health care profession.[104] Anesthesiologists and emergency room physicians rarely see patients in their own home, yet they need a home office for the same purposes as the taxpayer–doctor in *Soliman*.[105] Individuals in the construction trade are also affected because they too meet with clients at the job site and perform their trade and skills away from home.[106] The commentator also emphasized that

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95*Id.*

96*Id.* One of the most startling factors of the *Soliman* opinion is that it was 8 to 1 decision. In the majority and concurring with the majority were Justices Kennedy, White, O'Connor, Blackmun, Souter, Thomas, Scalia and Chief Justice Rehnquist. The lone dissenter was Justice Stevens, who emphasized that the Court's decision will again breed uncertainty in the law.

97Commissioner v. Soliman, 113 S. Ct. 701, 712 (1993) (Stevens, J., dissenting).

98*Id.*

99*Id.*

100*Id.* at 715.

101*Id.*

102See Meggard, *supra* note 3.

103*See* Robert T. Kelly Jr. *Home Office Deductions Restricted by Supreme Court*, 50 TAX'N FOR ACCT. 196 (1993).

104*Id.*

105*Id.*

106*Id.*

professors, artists and salesmen will suffer because they perform the majority of their services away from home.[107]

Because this criticism of the *Soliman* rule is well-taken, the better rule to follow regarding the principal place of business of a taxpayer is the rule set forth in the Court of Appeals opinion in the *Soliman* case.[108] The key element in the Court of Appeals test, as noted by Justice Stevens, is the requirement that no other office be available to the taxpayer.[109] This element benefits those taxpayers who need an office in their home to conduct necessary office functions connected with their trade or business. This requirement also prevents taxpayer abuse because there simply cannot be another office available to the taxpayer. For example, the lawyer who maintains a home office in addition to his regular office will be denied the deduction; and, he will be unable to reap the benefits of deducting the expenses related to his home office. Therefore, the facts-and-circumstances test is the better method for determining the home office deduction.

The following hypothetical fact patterns demonstrate the injustices of the new *Soliman* decision. For example, consider the professional house painter who maintains a home office. His in-office activities would consist of the following:

1. Billing customers and issuing statements;
2. scheduling painting crews;
3. scheduling painting times;
4. contacting and contracting with suppliers by phone;
5. contacting customers; and
6. writing estimates.

The out-of-office activities would consist of:

1. On site estimates;
2. scraping;
3. filling;
4. priming; and
5. painting.

Under *Soliman*, a court would first consider whether the home office was exclusively used for his trade or business. For purposes of this hypothetical, it is assumed that the painter would fulfill this requirement. The court would next consider the relative importance of each of the locations of the business activities. Undoubtedly, a court following the *Soliman* rule would find that the actual painting activities constitute the principal place of business, just as the location of the administration of anesthetics constitutes the principal place of business of the physician in *Soliman*.[110] In addition, the time factor would

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[107] *See supra* notes 3, at 103.

[108] Soliman v. Commissioner, 935 F.2d 52 (4th Cir. 1991).

[109] Commissioner v. Soliman, 113 S. Ct. 701, 712 (1993) (Stevens, J. dissenting).

[110] *Soliman*, 113 S. Ct. at 708. The actual treatment was the most siginificant event in the professional transaction.

weigh toward the out-of-office activities, because the actual preparation and painting take longer than scheduling and billing. Therefore, under the *Soliman* rule, the taxpayer in this hypothetical would be denied the deduction.

Under the Court of Appeals facts-and-circumstances test, the painter would be allowed a deduction for his home office expenses. First, a court would determine that his office was essential to his painting business because without it he could neither perform nor run his business. Second, a court would determine that the amount of time spent there would be substantial enough to satisfy the time element. The most important factor, if not the controlling factor, of this test—no other location available to perform the functions of business—would also be fulfilled because there is no other office available to the professional painter. The painter would therefore receive the deduction he is entitled to under the Code.[111]

Comparing the two tests reveals that each will provide the same end result only if the taxpayer works exclusively out of his home. For example, if the taxpayer claiming a home office deduction was an attorney working exclusively out of his home, there would be no change in the end result. Under *Soliman*, the attorney would receive the deduction because of the relative importance of the activities performed in his office and the amount of time spent in the office.[112] Similarly, under the Court of Appeals test, the attorney also would be allowed the deduction if he has no other office for his law practice.[113]

The foregoing hypotheticals exemplify the administrative inconsistencies that will result from the *Soliman* decision. Under *Soliman*, an attorney or an accountant would almost always receive the home office deduction, whereas the painter or landscaper will not receive the deduction. Since the purpose behind the tax code is to provide efficient, equal and fair rules and guidelines for taxation, the better test to follow in order to determine the principal place of business for the taxpayer is the Fourth Circuit Court of Appeals facts-and-circumstances test. Specifically, the provision that requires no other available office guarantees an efficient, fair and equal administration of the home office deduction section. This provision will also silence the fear that the Tax Court, federal courts and Congress have of the possibility for taxpayer abuse.

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[111] An analysis of a hypothetical involving an on-site custom cabinet maker or a landscaper would result in the same conclusions reached in the painter examples.

[112] The in-office activities would consist of meeting with clients, conducting research, writing briefs, motions, memoranda, and continuing legal education.

[113] An example involving an accountant or a real estate appraiser would also result in the same conclusions reached in the attorney example.

VI. CONCLUSION: WHAT IS LEFT OF THE HOME OFFICE DEDUCTION?

Since the *Soliman* decision the Tax Court has had at least three opportunities to modify or criticize the new home office test.[114] The three opinions, which are discussed below, indicate that the Tax Court is neither ready nor willing to challenge the authority of the Supreme Court. It appears from these opinions that the Tax Court will continue to accept the new test, despite its previous formulation of the equitable facts–and–circumstances test.[115]

On April 29, 1993, just three months after *Soliman*, the Tax Court accepted the Supreme Court's new subjective test to determine the availability of a home office deduction.[116] The pertinent issue in *Crawford* was whether the taxpayer was entitled to a home office deduction for the 1985 and 1986 tax years.[117] During these tax years, the taxpayer worked as an independent contractor in the medical field, providing emergency medical services for three to four local hospitals in Dallas, Texas.[118] In his home office, the taxpayer's activities consisted of follow–up work for patients, drafting correspondence and conducting other activities related to his medical practice.[119] The taxpayer spent approximately three to four hours in his home office for every ten hours spent at the hospitals.[120] The taxpayer's office was the largest room in the house and consisted of 20% of the total square footage.[121]

The Tax Court acknowledged the Supreme Court's rejection of the use of the availability of alternative office space as a factor in determining the principal place of business.[122] The Tax Court concluded that the taxpayer's home office was not his principal place of business, under the Supreme Court's subjective test, because he spent much more time at the hospitals than he did at home.[123]

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[114]Crawford v. Commissioner, 65 T.C.M. (CCH) 2540 (1993); Steines v. Commissioner, No. 91–3632, 1993 U.S. App. LEXIS, 12535 (7th Cir. Apr. 20, 1993); and Bowles v. Commissioner 65 T.C.M. (CCH) 2733 (1993).

[115]*See supra* note 114.

[116]Crawford v. Commissioner, 65 T.C.M. (CCH) 2540 (1993).

[117]*Id.* at 2541.

[118]*Id.*

[119]*Id.* at 2542.

[120]*Id.*

[121]65 T.C.M. (CCH) 2540, 2542 (1993). The taxpayer's office was furnished with the following items: private examination tables; storage cabinets for surgical tools and medicines; storage for patients' records; and business records and a small waiting area with chairs for the patients.

[122]*Id.* at 2544.

[123]*Id.* The Tax Court also addressed the "meeting and dealing with patients" exception set forth in I.R.C. § 280A(c)(1)(B), even though the taxpayer never raised the issue in his brief. The court stated that incidental meetings were not enough to qualify for this exception. Furthermore, the court found that the record failed to show the frequency

The Tax Court simply failed to criticize the Supreme Court's rejection of the more equitable rule that the Tax Court and Fourth Circuit Court of Appeals formulated.[124]

In two subsequent cases, the Tax Court and Seventh Circuit Court of Appeals followed the *Crawford* lead and did not criticize the *Soliman* decision. In *Steines v. Commissioner*, the Seventh Circuit Court of Appeals affirmed the Tax Court's reduction of a home office deduction.[125] The taxpayer claimed a deduction totalling 38.5% of his home and the Tax Court reduced the deduction to 7%.[126] The deduction was reduced because the Tax Court determined at trial that the taxpayer's first level living room area and "main" entry areas were not exclusively used for business purposes.[127] The Court of Appeals affirmed the findings of the Tax Court, finding no error.[128] More importantly the Court of Appeals again acknowledged the new *Soliman* test without criticizing it, parenthetically quoting *Soliman* as follows: "[the test] requires a comparative analysis of the various business locations, including analysis of the relative importance of functions performed at each location in light of the nature of the business."[129] The court simply failed to discuss *Soliman* any further.[130]

Finally, in *Bowles v. Commissioner*, the Tax Court again accepted *Soliman* without criticism.[131] The taxpayer in *Bowles* was a studio photographer, who worked for the Texas Youth Commission, teaching art to violent juveniles.[132] The taxpayer used his home office for drawing and preparing lesson plans and developing his photographs in the bathroom.[133] He deducted 1/7 of his expenses as constituting valid home office deductions, which were denied.[134] The court again followed *Soliman* and failed to criticize it.[135]The court concluded that his in-office activities were ancillary to the services he performed as a teacher with the Youth Commission.[136]

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and regularity of the visits by the patients to the taxpayer's home office. The deduction was denied based on this reason. *Id.*

124*See supra* note 108.

125No. 91-3632, 1993 U.S. App. LEXIS, 12435 (7th Cir. Apr. 20, 1993).

126*Id.*

127*Id.* at *7.

128*Id.*

129*Id.*

130*See supra* note 125.

13165 T.C.M. (CCH) 2733 (1993).

132*Id.*

133*Id.*

134*Id.*

135*Id.*

These three cases indicate that the Tax Court and Court of Appeals will neither challenge nor attempt to modify the *Soliman* rule in the near future. However, once the inequities of the United States Supreme Court's new test become apparent, then either the courts should modify the test or Congress should enact new legislation which reflects the better result dictated by the facts–and–circumstances test.

The *Soliman* decision still does not afford clear guidelines for determining the availability of a home office deduction. The only thing that has been accomplished is that deductions are denied for carpenters, landscapers, construction workers, doctors, professors, musicians, artists and sales professionals. Only a limited few are unharmed by the *Soliman* decision, such as lawyers and accountants. The clearest rule to follow for efficiency and fairness is the facts–and–circumstances test: The element requiring that no other office be available is essential.

The impact of *Soliman* requires tax–planners to carefully consider the ramifications of the decision. First of all *Soliman* involved only I.R.C. § 280A(c)(1)(A). Home office deductions are still available if a taxpayer meets or deals with clients in his home.[137] Second, the taxpayer can use a separate structure on his property as an office; but he may still have to satisfy the *Soliman* requirements.[138] One tax journal reports that the best method of planning is to keep accurate records and diaries of the time and activities spent with the business and to arrange business activities so that the taxpayer meets with clients in his home.[139]

In conclusion, the home office deduction is still available so long as there is adequate planning. The future of *Soliman* is uncertain, especially in light of the sound reasoning behind the facts–and–circumstances test. If the criticisms of *Soliman* continue, the Tax Court may again revert to this better standard in order to achieve efficiency, equality and most importantly, fairness. However, current decisions indicate that there will be no substantial change in the test in the near future.[140] Hopefully, the courts and Congress will realize the futility of the *Soliman* test and provide better guidance to the taxpayer. Time will tell.

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[136]65 T.C.M. (CCH) 2733, 2734 (1993).

[137]I.R.C. § 280(A)(c)(1)(B) provides in part: "as a place of business which is used by patients, clients, or customers in meeting or dealing with the taxpayer in the normal course of his trade or business."

[138]I.R.C. § 280(A)(c)(1)(C) provides in part: "separate structure which is not attached to the dwelling unit, in connection with the taxpayer's trade or business."

[139]See Kelly, *supra* note 103.

[140]*See* Crawford v. Commissioner, 65 T.C.M. (CCH) 2540 (1993); Steines v. Commissioner, No. 91–3632, 1993 U.S. App. LEXIS, 12535 (7th Cir. April 20, 1993); and Bowles v. Commissioner 65 T.C.M. (CCH) 2733 (1993).